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The Manufacturers Hanover
Financial Digest
Economic Commentary, Selected Financial Data, and Business Indicators

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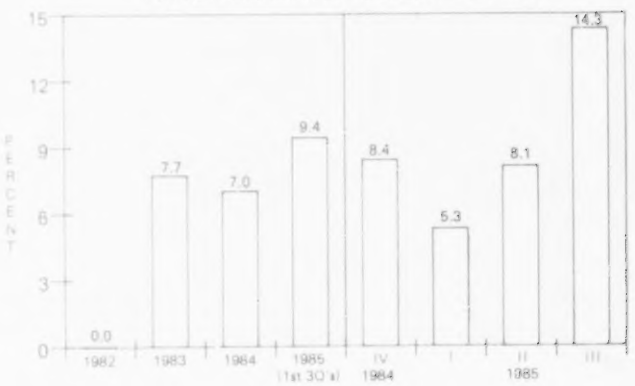
Monetary Policy . . .

Despite strong indications that today's monetary policy posture will remain essentially unchanged, and consequently that the Federal Reserve will not seek to aggressively push short-term interest rates lower, strong rallies persist in both the bond and stock markets. With oil prices slumping, prospects for lower inflation rates continue to send bond prices higher and yields in the opposite direction, while the likelihood of enhanced corporate profitability does the same for share prices. Not even the Congressional testimony of Fed Chairman Paul A. Volcker could dampen market enthusiasm for long; the markets took in stride the statements that no significant changes had recently been made in monetary policy and warnings of the potentially negative effects of too rapid a drop in the external value of the dollar. For while such comments may have dashed hopes of an imminent turn toward greater monetary ease, they don't preclude one forever—especially in light of the exceptionally good inflation rate outlook and the need of several high-debt, advanced developing countries for more interest rate relief.

One reason why the Fed may have decided to postpone further overt easing initiatives is the brightening business outlook. While there may be no boom on the horizon, there is certainly no bust, either. For one thing, recent trends in the index of leading economic indicators, payroll employment, housing starts and automobile sales all point to a strengthening pace of business. In January, payroll employment surged by more than 550,000, housing starts ran at their highest level in nearly two years, and automobile sales, stimulated by dealer financing incentives, ran at a better than nine million unit seasonally adjusted annual rate during the second ten-day selling period in February—one of the best levels since last autumn.

To be sure, such other signs as manufacturing employment, industrial production and nonauto retail sales do not paint quite as robust a picture. However, with domestic auto output running nearly ten percent ahead of the pace of last quarter, the trade deficit expected to narrow during the course of the year as a result of both the dollar's slide in the foreign exchange markets and a pickup in business activity in industrial Europe, and inventory spending poised to accelerate (Financial Digest—February 14, 1986), it appears a good bet that current business trends look good enough to preclude a quick turn toward ease.

FOREIGN INFLOWS AS A PERCENT OF TOTAL FUNDS RAISED IN CREDIT MARKETS



. . . Should Be In A Holding Pattern . . .

So, too, recent Federal budget developments could be an obstacle to more ease. The Federal District Court decision that certain provisions of the Gramm-Rudman-Hollings Deficit Reduction Act are unconstitutional clearly set back Federal budget balancing efforts and, although the ruling will be appealed, the initial decision certainly clouds prospects that a credible deficit reduction program will be put in place any time soon. What is more, the release of the President's budget for fiscal year 1987 reinforces such uncertainty, promising little in the way of fiscal relief. For although a red-ink total of less than $144 billion is projected, it relies on a rather upbeat set of economic assumptions which may or may not come to pass.

More immediately, however, the Federal deficit should top $200 billion once again in the current fiscal year, despite the fact that nearly $12 billion of Gramm-Rudman mandated spending cuts are embodied in the current budget. As a result, while the Fed may eventually have to loosen the monetary

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. . . In The Weeks Ahead

Selected Federal Reserve Data

	Week Ending 2/26/86	$ Change from Week Ago	$ Change from Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies			
Owned Outright & RPs		− 601	+16,167
Loans to Depository Inst		− 123	− 316
Float		+ 113	496
Total Reserve Bank Credit		− 1,338	+18,488
Treasury Deposits with			
Federal Reserve Banks		+ 766	+ 2,884
Currency in Circulation		− 511	+13,067
Gov'ts held for Foreign Acct. by F.R. Banks (End of Week)		1,953	−12,588
	2/26/86		
Member Bank Reserves			
Total Reserves Held		428	+ 5,325
Excess (Deficiency)		196	+ 191
Net Free Reserves		608	+ 168

Monetary Aggregates†		$ Change from Three Months Ago*	$ Change from Year Ago
M1 (2/17/86)		− 9.8‡	+ 11.0‡
M2 (January '86)		− 4.4	+ 6.9
M3 (January '86)		+ 6.0	+ 6.6
Domestic Nonfinancial Debt (3rd Q '85)		+ 11.7	+ 13.7

†Seasonally adjusted. *Seasonally adjusted annual rate. ‡Four-week moving average.

New York Money Market

Offering Rates 2/28/86	3 Months	6 Months	1 Year
†U.S. Treasury Bills	6.99%	6.99%	6.91%
* Federal Agencies	7.20	7.10	7.00
* Municipal Notes—High Grade (46% Taxable Equivalent)	8.06	8.52	8.89
Negotiable Time CDs			
Manufacturers Hanover		Rates By Arrangement	
* Secondary Market—Prime	7.55	7.55	7.55

†Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	7.55%	Mar.	7.65%
15- 29 days	7.55	Apr.	7.60
30- 59 days	7.60	May	7.50
60- 89 days	7.55	Jun.	7.45
90-179 days	7.48	Jul.	7.35
180-239 days	7.35	Aug.	7.25
240-270 days	7.35		

†Industrial Paper—Prime			
30- 89 days	7.53%	†Federal Funds	
90-120 days	7.40	Effective Rate	7.94%

†Discount basis. *Subject to availability. ‡Estimated.

Selected Business Indicators

	Latest Period	Previous Period	Year Ago Period
Gross National Product (Current Dollars)*		$ 4,017	$ 3,853
Gross National Product (1982 Dollars)*		$ 3,584	$ 3,516
Percent Change, Annual Rate		3.0	0.6
Change in Consumer Prices*		4.8%	2.4%
Change in Producer Prices*		6.0%	− 1.2%
Civilian Employment (Thousands of Persons)†		108,206	106,315
Unemployment as % of Civilian Labor Force†		6.9%	7.4%
Personal Income*		$ 3,386r	$3,217
Leading Indicators Composite Index (1967=100)†		172.0	164.1
Industrial Production Index (1977=100) †		126.3	123.6
Net Change in Consumer Installment Credit †		$ 4.79	$ 6.82
U.S. Merchandise Trade Balance †		− $ 15.15r	− $ 11.57r
Plant and Equipment Expenditures*		$388.98(a)	$371.16
Private Housing Starts (Thousands of Units)*		1,804r	1,804
New Construction Expenditures*		$ 344.8	$ 310.1
Total Business Inventories †		$ 582.8	$ 573.4
Total Business Sales †		$ 432.0	$ 421.6

*Seasonally adjusted annual rate. †Seasonally adjusted. r-Revised. a-Anticipated.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (2/12/86)	186,854	+ 480	+ 8,692
New York City (2/19/86)	72,316	+ 67	+ 3,738
Commercial Paper (2/19/86)	299,858	+ 24	+50,809

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (2/12/86)	255,914	+ 92	+ 3,142
New York City (2/19/86)	67,983	+ 168	– 2,943

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (2/12/86)	715,878	– 4,294	+ 58,909
New York City (2/19/86)	159,188	+ 5,024	+ 18,167

Financial Markets

	Friday 2/28/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90 Day Bills†	5.52%	0	– 1.60
180 Day Bills†	5.78%	– .08	– 1.99
Longest Bills†	7.67%	– .14	– 2.33
Recent Issues:			
8s 2/29/88	7.84%	.23	
8¾s 12/31/89	7.94%	.27	
8⅞s 2/15/96	8.09%	.39	
9¼s 2/15/16	8.23%	.43	
Municipals:			
Bond Buyer–20 Bond Index* (2/27/86)	7.56%	.46	– 2.73
Blue List Total ($ Million)	$7,340	– $148	$ 509
30-Day Visible Supply ($ Million)	$5,315	+ $368	$1,553
Total	$7,565	+ $220	– $2,068
Corporates:			
Moody's Aa Composite (2/27/86)	9.74%	.42	3.10
30-Day Visible Supply ($ Million)	$7,134	+ $799	$16
Stocks:			
Dow Jones Averages:			
Industrials	1,568.55	+ 11.35	+ 409.70
Transportation	592.29	5.46	+ 156.96
Utilities	165.83	.30	+ 37.03
65 Stocks	674.61	+ 1.59	+ 151.50
N.Y.S.E. Composite Index	130.74	+ 1.33	+ 24.70
N.Y.S.E. Avg. Daily Vol. for Week (000's)	165,152	+ 7,762	+ 54,566

* 46% Taxable equivalent 12.93%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 2/28/86	Week Ago
Overnight	7.75%	7.81¼
1 month	7.75	7.88
3 month	7.69	7.88
6 month	7.69	7.88
1 year	7.75	8.00
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	8.50	8.70%
Long Term (7 to 15 yrs.)	8.90	9.15

FOREIGN EXCHANGE SPOT RATES New York Opening (2/28/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02199	45.48
Canada	7007	1.4272
Denmark	1219	8.2050
France	1466	6.8227
Germany	4508	2.2185
Italy	0006618	1511.00
Japan	005556	179.99
Mexico	.002116	472.50
Netherlands	3987	2.5079
Switzerland	5340	1.8725
U.K.	1.4653	.6825

"Before we had INTERPLEX, simple tasks like pulling balances were often a nightmare."

Raymond Kean
Treasury Manager
Ameritech Services

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